DEPARTMENT OF STATE REVENUE

04-20120393.LOF

Letter of Findings Number: 04-20120393
Use Tax
For Tax Year 2009

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ISSUES

I. Use Tax–Recreational Vehicle.

Authority: Gregory v. Helvering, 293 U.S. 465 (1935); Comm'r v. Transp. Trading & Terminal Corp., 176 F.2d 570 (2d Cir. 1949); Horn v. Comm'r, 968 F.2d 1229 (D.C. Cir. 1992); Lee v. Comm'r, 155 F.3d 584 (2d Cir. 1998); IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-8.1-5-1; 45 IAC 2.2-3-4.

Taxpayer protests the imposition of use tax on the use of a recreational vehicle.

II. Tax Administration–Negligence Penalty.

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2.

Taxpayer protests the imposition of a ten percent negligence penalty.

STATEMENT OF FACTS

Taxpayer is an individual and is a resident of Indiana. The Indiana Department of Revenue ("Department") determined that on January 24, 2009, Taxpayer purchased a recreational vehicle ("RV") in Florida and had been using the RV in Indiana and other states without paying sales tax in any jurisdiction. As a result, the Department issued proposed assessments for Indiana use tax, ten percent negligence penalty, and interest. Taxpayer protests that the RV was purchased and titled by a Montana LLC, of which Taxpayer was the sole member, that the RV was purchased, used and stored in Florida, and that no Indiana sales or use tax is due. Taxpayer also protests the imposition of negligence penalty. An administrative hearing was conducted and this Letter of Findings results. Further facts will be supplied as required.

I. Use Tax–Recreational Vehicle.

DISCUSSION

Taxpayer protests the imposition of use tax on the use and storage of an RV in Indiana. The Department imposed use tax after determining that Taxpayer had been using and storing the RV in Indiana and that no sales tax had been paid on the purchase of the RV. Taxpayer protests that the RV was titled by a Montana LLC and that all legal documents establishing the existence of the LLC were properly filed in Montana. Also, Taxpayer states that the RV was never brought into Indiana, but rather was purchased, used, and stored in Florida. The Department notes that the burden of proving a proposed assessment wrong rests with the person against whom the proposed assessment is made, as provided by IC § 6-8.1-5-1(c).

The sales tax is imposed by IC § 6-2.5-2-1, which states:

(a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana.

(b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state.

The use tax is imposed under IC § 6-2.5-3-2(a), which states:

(a) An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

Also, 45 IAC 2.2-3-4 provides:

Tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used, or otherwise consumed in Indiana is subject to Indiana use tax for such property, unless the Indiana state gross retail tax has been collected at the point of purchase.

Therefore, when tangible personal property is acquired in a retail transaction and is stored, used, or consumed in Indiana, Indiana use tax is due if sales tax has not been paid at the point of purchase. The Department determined that Taxpayer purchased the RV in Florida in a retail transaction on January 24, 2009, but did not pay Florida sales tax on the purchase. The Department therefore issued proposed assessments for Indiana use tax.

Other than the purchase of the RV, Taxpayer was unable to provide any documents establishing any LLC business or non-business activity at all in Indiana, Montana, or any other state in the union. While the LLC made no attempt to undertake any further activity, the titling of the RV by the LLC did have a significant impact on Taxpayer's sales taxes. This leads to consideration of the "sham transaction" doctrine, which is long established both in state and federal tax jurisprudence dating back to Gregory v. Helvering, 293 U.S. 465 (1935). In that case, the Court held that in order to qualify for favorable tax treatment, a corporate reorganization must be motivated by

the furtherance of a legitimate corporate business purpose. Id. at 469. A corporate business activity undertaken merely for the purpose of avoiding taxes was without substance and "[T]o hold otherwise would be to exalt artifice above reality and to deprive the statutory provision in question of all serious purpose." Id. at 470.

The courts have subsequently held that "in construing words of a tax statute which describe [any] commercial transactions [the court is] to understand them to refer to transactions entered upon for commercial or industrial purposes and not to include transactions entered upon for no other motive but to escape taxation." Comm'r v. Transp. Trading & Terminal Corp., 176 F.2d 570, 572 (2d Cir. 1949), cert. denied, 338 U.S. 955 (1950). "[T]ransactions that are invalidated by the [sham transaction] doctrine are those motivated by nothing other than the taxpayer's desire to secure the attached tax benefit" but are devoid of any economic substance. Horn v. Comm'r, 968 F.2d 1229, 1236-7 (D.C. Cir. 1992). In determining whether a business transaction was an economic sham, two factors can be considered; "(1) did the transaction have a reasonable prospect, ex ante, for economic gain (profit), and (2) was the transaction undertaken for a business purpose other than the tax benefits?" Id. at 1237. The question of whether or not a transaction is a sham, for purposes of the doctrine, is primarily a factual one. Lee v. Comm'r, 155 F.3d 584, 586 (2d Cir. 1998).

In this case, the facts are that the Montana LLC had no business or non-business functions and never attempted to acquire, maintain, or dispose of any property other than the RV in question. In fact, the LLC had no functions of any kind other than those directly related to the purchase of the RV in question. The titling of the RV in Montana, a state without a sales tax, was merely an attempt to reduce or eliminate Taxpayer's sales and use tax liabilities. The formation of the LLC and the titling of the RV in the name of the LLC was therefore a "sham transaction."

In conclusion, Taxpayer never intended for the LLC to have any valid functions beyond avoiding sales and use taxes on the purchase of the RV. Therefore, the formation of the LLC and the titling of the RV by the LLC was a sham transaction. Consequently, Taxpayer acquired tangible personal property in a retail transaction, used and stored it in Indiana, but did not pay sales tax at the point of purchase or anywhere else. Taxpayer submitted documentation which established the existence of the RV parks at which Taxpayer claimed the RV was used and stored, but Taxpayer did not submit documentation such as invoices for RV lot rental or utility usage to establish that the RV was actually used and stored there. In such circumstances, Indiana use tax is due, as explained by 45 IAC 2.2-3-4.

FINDING

Taxpayer's protest is denied.

II. Tax Administration–Negligence Penalty.

DISCUSSION

The Department issued a proposed assessment and the ten percent negligence penalty for the tax years in question. Taxpayer protests the imposition of penalty and states that the RV discussed in Issue I was used in Florida and not in Indiana. The Department refers to IC § 6-8.1-10-2.1(a), which states in relevant part:

> If a person:
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> . . .
>
> (3) incurs, upon examination by the department, a deficiency that is due to negligence;
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> . . .
>
> the person is subject to a penalty.

The Department refers to 45 IAC 15-11-2(b), which states:

> Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.
>
> (Emphasis added.)

45 IAC 15-11-2(c) provides in pertinent part:

> The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section.

In this case, Taxpayer incurred an assessment which the Department determined was due to negligence under 45 IAC 15-11-2(b), and so was subject to a penalty under IC § 6-8.1-10-2.1(a). After a review of the circumstances in this case, Taxpayer has established that the assessment arose due to reasonable cause and not due to negligence, as required by 45 IAC 15-11-2(c). Therefore, the negligence penalty will be waived.

FINDING

Taxpayer's protest is sustained.

SUMMARY

Taxpayer is denied on Issue I regarding the imposition of use tax on the purchase of a recreational vehicle. Taxpayer is sustained on Issue II regarding imposition of penalty.

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